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November 16, 2015

Hon. Jeff DeWit
Arizona State Treasurer
1700 W. Washington Street, 1st Floor
Phoenix, Arizona 85007

Re: Opinion on HCR 2001, 52nd Leg., 1st Spec. Sess.

Dear Mr. Treasurer:

You have engaged this firm to perform an analysis of HCR 2001 to determine whether it conflicts with the Arizona Enabling Act, as amended Dec. 7, 1999, H.R. 747, 113 Stat. 1682, or violates the single-subject rule, and if either be the case, whether you have any legal rights to sue to prevent HCR 2001 from being placed on the special election ballot for May 17, 2016. HCR 2001 proposes a measure to Arizona voters to amend both art. 10, § 7, and art. 11 of the Arizona Constitution. If approved by the voters, the proposed amendment of art. 10, § 7, will change the formula for annual distribution of funds ("Distribution Formula") from the Arizona Permanent Land Endowment Trust Fund ("Trust"), and the proposed amendment of art. 11 will add § 11 that will alter the formula for annual inflation-based adjustments of school aid required by A.R.S. § 15-901.01.

OPINIONS

After performing the requested analysis, we have formed the following opinions:

1) An amendment to the Distribution Formula, if passed by the voters at the special election, cannot become effective until and unless Congress revises the Enabling Act to approve the amendment. Congress established the Trust in the

Enabling Act, and the Act's terms bind the State of Arizona and overrule any part of the Arizona Constitution or Arizona laws that conflict with such terms.

2) Arizona courts will reject a pre-election lawsuit founded on the argument that HCR 2001 conflicts with the Enabling Act. The rejection will be based on the separation-of-powers doctrine preventing courts from interfering with the process of legislating, and on the ripeness doctrine precluding them from intervening until a measure actually has been passed.

3) Courts will consider a pre-election challenge based on the single-subject rule, if filed within the 20-day deadline set by A.R.S. § 19-161, but the chances of success based on the single-subject rule are sufficiently in doubt in this case to counsel against filing a lawsuit based on that rule alone. The single-subject rule prevents the Legislature from proposing a measure to the voters that embraces more than one subject. To comply with this rule, the various parts of a referred measure must be "topically related" and must so interrelate as "to form a consistent and workable proposition." One can make an argument that HR 2001 fails both prongs of the test, but the case for failing the second prong is the stronger. Regardless, in our view, neither is strong enough to justify going into court in view of the risks involved.

4) If the voters approve the referred measure at the special election, you would have grounds to file a lawsuit to have the amendment altering the Distribution Formula declared ineffective until Congress amends the Enabling Act to accommodate the changes in the Distribution Formula. It is a judgment call whether to file such a post-election lawsuit in view of the fact that, if the Arizona delegation can push an amendment to the Enabling Act through Congress to authorize the changes to the Distribution Formula proposed by HCR 2001, it would make a successful lawsuit and resulting judgment moot and perhaps a pyrrhic victory at best.

ANALYSIS

A. HCR 2001 Conflicts with the Current Enabling Act.

1. The Enabling Act Establishes the Trust and Governs Its Administration.

Congress established the Trust in 1910 in sections 24-30 of the Enabling Act, and therein confirmed an earlier grant of lands to the Territory of Arizona and granted additional lands to the State of Arizona, making a total conveyance of approximately 8,239,419.53 acres of land at statehood, to be held in trust for the support of Arizona public schools. *Murphy v. State*, 65 Ariz. 338, 361, 181 P.2d 336, 351 (1947). Congress made lesser conveyances of public land to the State of Arizona in trust for multiple other purposes. *Id.*

In 1911, the people of Arizona adopted the Arizona Constitution, and art. 20, §§ 12 and 13 thereof, irrevocably accepted the Enabling Act's trust conditions. *Fain Land & Cattle Co. v Hassell*, 163 Ariz. 587, 589, 790 P.2d 242, 244 (1990). Thus, federal law is "supreme in this field," and neither "the legislature, nor the people may alter or amend the trust provisions contained in the Enabling Act without congressional approval." *Kadish v. Arizona State Land Dept.*, 155 Ariz. 484, 486, 747 P.2d 1183, 1185 (1987). Any "statute or amendment to the state Constitution in conflict therewith is null and void." *Boice v. Campbell*, 30 Ariz. 424, 428, 248 P. 34, 35 (1926). Though the Legislature cannot adopt provisions governing the Trust that loosen the Enabling Act's conditions, it can adopt more restrictive provisions for the Trust's protection. *Fain*, 163 Ariz. at 595, 790 P.2d at 250.

Based on sad experience with lands conveyed in trust to other states, which the Arizona Supreme Court chronicled in *Murphy*, 65 Ariz. 350-51, 181 P.2d at 344, Congress intended in the Enabling Act "to severely circumscribe the power of state government to deal with the assets of the common school trust." *Kadish v. Arizona State Land Dept.*, 155 Ariz. 484, 487, 747 P.2d 1183, 1196 (1987). Thus, Congress imposed duties upon the State of Arizona "of a trustee and not simply the duties of a good business manager." *Id.*

2. Arizona Mismanages the Trust.

Despite such limitations on the State's power to deal with Trust lands, as early as 1915 the State began to mismanage the Trust, eventually resulting in the loss of millions of dollars in improvident agricultural loans. *Murphy*, 65 Ariz. at 355-56, 181 P.2d at 347-48. The Arizona Supreme Court described this unfortunate turn of events as follows:

> In view of the dissipation of land grants by the various states prior to the admission of Arizona and New Mexico, we submit that it was not merely prophetic to anticipate that the legislature would submit to pressure groups and enact legislation encouraging and licensing the state treasurer, governor, and secretary of state to invest the permanent funds in questionable investments, but rather it was a certainty that such attempts would be made. Prophetically or realistically, it came to pass in Arizona.

Id. at 355, 181 P.2d at 347.

3. Arizona Courts Interpret the Enabling Act Cautiously and Conservatively.

As a result, Arizona courts have been vigilant in enforcing the conditions set forth by the Enabling Act. To illustrate, Arizona courts will "not permit use of trust lands or their proceeds in ways not expressly authorized, even if doing so would benefit the trust." *Rumery v. Baier*, 231 Ariz. 275, 279, ¶ 21, 294 P.3d 113, 117 (2013). In the same vein, courts "strictly apply the Enabling Act's restrictions regarding disposal of school trust assets." *Kadish*, 155 Ariz. at 488, 747 P.2d at 1187. Similarly, all doubts "must be resolved in favor of protecting trust purposes." *Id.* at 495, 747 P.2d at 1194.

4. Congress Amends the Enabling Act as Times and Conditions Change.

At the prompting of the Arizona delegation, Congress periodically has amended the Enabling Act to allow more flexible use of Trust land. *Deer Valley Unified School District No. 97 of Maricopa County v. Superior Court in and for Maricopa County*, 157 Ariz. 537, 539, 760 P.2d 537, 539 (1988). "In each case,

the Arizona electorate voted to change the Arizona Constitution to take advantage of the prior revision in the federal statutory law." *Id.*

5. Congress Approves Arizona's Adoption of the Distribution Formula.

In 1998, the Legislature referred an amendment to ARIZ.CONST, art. 10, § 7, to the voters in the form of Proposition 102, which was approved at the 1998 general election. This measure is found in the Secretary of State's publicity pamphlet at http://apps.azsos.gov/election/1998/Info/PubPamphlet/prop102.pdf. Among other things, Prop. 102 permitted investment of a portion of the Trust in equities, established a formula for distributions from the Trust based on investment performance and inflation averaged over the preceding five years, and made an exception for specified years in which the distribution was set at a flat annual rate of two and a half percent.

The 1998 measure did not have prior approval from Congress, which deviated from the State's prior practice, noted in the quote from the *Deer Valley Unified School District* opinion, of first obtaining Congress's approval before amending the Arizona Constitution to ease restrictions governing the administration of the Trust. The analysis of the Legislative Council published in the 1998 publicity pamphlet warned voters of the need for congressional approval:

> In order for this proposal to become fully operative, the United States Congress will also have to amend the state Enabling Act to allow all earnings, including capital gains and dividends as well as interest, to be distributed from the permanent funds to the trust beneficiaries.

At any rate, in 1999, Congress granted approval of the Legislature's 1998 amendment. H. Rept. 106-140 stated the purpose of Congress's amendments of the Enabling Act granting such approval as follows:

> The purpose of H.R. 747 is to protect the permanent trust funds of the State of Arizona from erosion due to inflation and modify the basis on which distributions are made from those funds.

Congress specifically noted that the distribution of all annual income earned by the Trust, as had been required before the 1999 amendments, had the effect, when coupled with inflation, of eroding the real value of the Trust corpus:

> As currently provided for in the original Enabling Act, the Funds must pay out all of their income, with "income" interpreted as all interest and dividends received. This creates a problem because it does not account for and adjust to rates of inflation. Inflation has averaged approximately 4.5% over the past 50 years and the income generated from the Funds has grown at less than the rate of inflation. To account for inflation, a portion of the interest should be retained and reinvested to fuel future income growth.

As a result, Congress added the following provisions to the Enabling Act as part of the 1999 amendment:

> The trust funds (including all interest, dividends, other income, and appreciation in the market value of assets of the funds) shall be prudently invested on a total rate of return basis. Distributions from the trust funds shall be made as provided in Article 10, Section 7 of the Constitution of the State of Arizona.

P.L. 106-133, 106th Cong., 113 Stat. 1682, § 2(a) (Dec. 7, 1999).

6. Congress's Approval of the Distribution Formula in 1999 Did Not Blanketly Authorize the Legislature to Alter the Formula at Its Discretion.

One effect of this provision of the 1999 amendment was to adopt the Distribution Formula, set forth in Prop. 102, into the Enabling Act by reference, but in our opinion the 1999 amendment did not give the Legislature authority later to amend ARIZ.CONST. art. 10, § 7, to increase annual distributions beyond the Distribution Formula without Congress's approval. We base this opinion on two grounds: (a) Congress's expressed intent, and (b) the applicable rules of statutory construction.

Regarding Congress's intent, a grant of such broad authority is found nowhere in the 1999 amendment's legislative history or the statement of congressional intent set forth in H. Rept. 106-140.

Construing Congress's 1999 amendment to give the Legislature unfettered authority to change the Distribution Formula, even with voter approval, obviously could lead to improvident dissipation of the Trust, contrary to the congressional intent stated in H. Rept. 106-140 that a "portion of the interest should be retained and reinvested to fuel future income growth."

Invasion of Trust corpus is also inconsistent with prior case law and appears to run contrary to the State's practice of distributing only income, at least since the Arizona Supreme Court's 1947 decision in the *Murphy* case decrying the profligate investments made in the first decades of the Trust's existence.

Nonetheless, in 2012, the Legislature referred another measure to the voters, denominated Prop. 118, which amended art. 10, § 7, to set the distribution rate from the Trust, for fiscal years 2012-13 through 2020-21, at two and a half percent of the Trust's preceding five-year average monthly market values. Interestingly, this time the Legislative Council's analysis did not note the need for congressional approval of this amendment before it could take effect.

To date, Congress has not approved the 2012 revisions to the rate of distribution from the Trust made by Prop. 118, which calls their effectiveness into question. In our view, the only way Prop. 118 survives judicial scrutiny is if, following *Fain*, 163 Ariz. at 595, 790 P.2d at 250, it makes a more restrictive rate of distribution than what already is permitted by the 1998 amendment to art. 10, § 7, approved by Congress in 1999.

Moving forward to HCR 2001, if Congress were dissatisfied, as expressed in H. Rept. 106-140, with the State's pre-1999 practice of distributing all income and thus allowing the real value of the Trust corpus to erode over time due to inflation, it hardly can be argued that it would comply with Congress's expressed intent to adopt an amendment of the Distribution Formula that goes further to allow distribution of Trust corpus, even if limited to no more than a decade's duration, as HCR 2001 would do.

Turning to the rules of statutory construction regarding one law adopting the provisions of another by reference, while it has its exceptions, the basic rule is that the "adoption takes the statute as it exists at the time of adoption and does not

include subsequent additions or modifications by the statute so taken unless it does so by express intent." *Hassett v. Welch*, 303 U.S. 303, 313-14 (1938).[1]

Other cases would expand this rule and draw a distinction between "statutes of specific reference" and "statutes of general reference." *Pearce v. Director, Office of Workers' Compensation Programs, U.S. Dept. of Labor*, 603 F.2d 763, 767 (9th Cir. 1979). A law that refers to specific provisions of another law and adopts them by reference is considered a statute of specific reference and does not adopt later amendments to the incorporated law. *Id.* In contrast, a law that refers to the "general law on a given subject" is deemed to adopt later amendments to the incorporated law as well. *Id.*

Thus, we conclude that, with respect to its adoption of the Distribution Formula as established by Prop. 102 in 1998, Congress's 1999 amendment of the Enabling Act was a law of specific reference. It adopted no more than limited and specific provisions from Prop. 102: "Distributions from the trust funds shall be made as provided in Article 10, Section 7 of the Constitution of the State of Arizona." This conclusion is consistent with, and is buttressed by, the intent expressed by Congress in H. Rept. 106-140 of building back the Trust corpus after decades of the erosion of its real value caused by inflation.

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[1] Because the Enabling Act is federal law, it is best to rely on federal precedents dealing with its interpretation. Nonetheless, we note that, if we were dealing with an Arizona law, the rules of statutory construction are less clear, but at any rate still focus primarily on legislative intent. The Arizona Supreme Court once held that the "Arizona Legislature can incorporate by reference only such laws and regulations as exist at the time they enact legislation and cannot constitutionally adopt future changes which might occur." *Scappaticci v. Southwest Sav. and Loan Ass'n*, 135 Ariz. 456, 460, 662 P.2d 131, 135 (1983). More recently, the Arizona Supreme Court declined to follow this rule, without specifically discussing the *Scappaticci* case, preferring to focus on legislative intent to determine whether a law incorporating another law by reference also includes later amendments of the incorporated law. *Arizona Clean Elections Com'n v. Brain*, 234 Ariz. 322, 328, ¶ 27, 322 P.2d 139, 145 (2014). We are content to rest our conclusion on the congressional intent expressed in H. Rept. 106-140, noted above.

7. HCR 2001 Cannot Take Effect without Congress's Approval.

For the foregoing reasons, we have formed the opinion that HCR 2001, even if approved by the voters at the May 17, 2016, special election, cannot take effect without Congress's amendment of the Enabling Act to accommodate the changes HCR 2001 would make in the rate of distribution from the Trust, unless, again consistent with *Fain*, the new rate of distribution is more restrictive than what Congress approved in 1999. Specifically, HCR 2001 must be consistent with Congress's intent, expressed in H. Rept. 106-140, of reinvesting income to fuel future growth, failing which HCR 2001 will require specific authorization from Congress to become effective.

B. Courts Will Reject a Pre-Election Challenge to the Substance of HCR 2001.

Arizona courts will not interfere with a measure referred by the Legislature to a vote of the people based on whether its substance is valid or constitutional. *League of Arizona Cities and Towns v. Brewer*, 213 Ariz. 557, 559, ¶ 8, 146 P.3d 58, 60 (2006); *Queen Creek Land & Cattle Corp. v. Yavapai County Board of Supervisors*, 108 Ariz. 449, 452, 501 P.2d 391, 394 (1972); *State v. Osborn*, 16 Ariz. 247, 250, 143 P. 117, 118 (1914). A substantive challenge must follow the election. *Id.*

Three reasons have been given for such judicial restraint: 1) separation of powers, *id.*, 2) ripeness, that is that the voters could always vote no, making a court's consideration of the measure unnecessary and moot, *Winkle v. City of Tucson*, 190 Ariz. 413, 415, 949 P.2d 502, 504 (1997), and 3) courts decline to give advisory opinions before a measure is adopted. *Id.*

An exception to this principle is made for a proposed amendment to the state constitution that involves a violation of the single-subject rule. *Tilson v. Mofford*, 153 Ariz. 468, 471-72, 737 P.2d 1367, 1370-71 (1987).

In the case of an initiative, further exceptions are made for defects in the form of the petition, *Inman v. Bolin*, 98 Ariz. 358, 364-65, 404 P.2d 705, 709 (1965), insufficient signatures, *id.,* measures that do not involve legislation, *Respect Promise in Opposition to R-14-02-Neighbors for a Better Glendale v. Hanna*, __ P.3d __ , 2015 WL 5474447, * 4-5, ¶¶ 4-5 (Ariz.App., Sept. 18, 2015),

pre-election challenges specifically authorized by law, and, at the local level, zoning ordinances. *City of Scottsdale v. Superior Court in and for Maricopa County*, 103 Ariz. 204, 209, 439 P.2d 290, 293 (1968).

C. Whether HCR 2001 Violates the Single-Subject Rule Is Too Close a Question to Warrant a Pre-Election Lawsuit.

As noted above, the single-subject rule forms grounds to file a pre-election lawsuit against a constitutional amendment proposed to Arizona voters. *Tilson*, 153 Ariz. at 471-72, 737 P.2d at 1370-71 (1987).

The Arizona Supreme Court most recently stated the single-subject rule as follows: "This test requires us to consider (1) whether a proposition's provisions are *topically related*, and (2) whether they are *sufficiently interrelated* so as to form a consistent and workable proposition." *Save Our Vote, Opposing C-03-2012 v. Bennett*, 231 Ariz. 145, 149-50, 291 P.3d 342, 346-47 (2013) (italics in original, internal quotation marks omitted.)

Proposed art. 10, § 7, and art. 11, § 11, are topically related only in the broad sense that both deal with school finance, though in very different ways. Art, 10, § 7, relates to the Trust, a source of support of the public schools. Art. 11, § 11, changes the trigger for when the Legislature must provide inflation-based adjustments of school funding. They have little to do with each other, except that they both involve school funding -- art. 10, § 7, as a source of funds, and art. 11, § 11, as a trigger for increasing funds to be expended on schools. What's more, as noted above, the Trust includes multiple grants made by Congress for purposes other than the support of public schools.[2] The proposed alteration of the Distribution Formula would change the distributions made for their purposes as

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[2] At statehood, for "the use and benefit of the common schools, there was granted approximately 8,239,419.53 acres; for university purposes 200,000 acres; for legislative, executive, and judicial public buildings 100,000 acres; for penitentiary 100,000 acres; for insane asylums 100,000 acres; for schools and asylums for the deaf, dumb, and blind 100,000 acres; for miners' hospitals for disabled miners 50,000 acres; for normal schools 200,000 acres; for state charitable, penal, and reformatory institutions 100,000 acres; for agricultural and mechanical colleges 150,000; for school of mines 150,000 acres; and for military institutes 100,000 acres." *Murphy*, 65 Ariz. at 361, 181 P.2d at 351.

well. To the extent the proposed amendment relates to the other beneficiaries, the two sections are not topically related.

Concerning interrelatedness, the Supreme Court has described the determinative test as follows:

> This rule does not require that all components of a provision be logically dependent on one another. Instead, we measure the provisions against objective factors, such as whether various provisions are facially related, whether all the matters addressed by an initiative concern a single section of the constitution, whether the voters or the legislature historically has treated the matters addressed as one subject, and whether the various provisions are qualitatively similar in their effect on either procedural or substantive law. Although these factors are not exclusive and might not all apply in a particular case, they guide our analysis.

Save Our Vote, 231 Ariz. at 150, ¶ 15, 291 P.3d 347 (internal citations and quotation marks omitted.)

A case can be made that HCR 2001 flunks several of these factors. The two are facially related only in the broadest sense, and then only to the extent schools are involved. To the extent the Distribution Formula amendment would affect other beneficiaries, there is no interrelatedness. Further, they do not involve even the same article of the Arizona Constitution, much less the same section. This is the first time an amendment of the Distribution Formula has been linked to an amendment of the annual inflation-adjustment requirement. They are not similar in their respective effects on procedural or substantive law. They are similar only in the sense that the proposed increased distributions from the Trust will allow increases to be made to annual school funding, including inflation-related funding, without the need of a tax increase.

All that said, the single-subject rule has experienced very uneven application by Arizona courts, which historically have been reluctant to prevent an election on this basis. We can see a court holding that HCR 2001 falls sufficiently within the broad topic of school finance and that the amendments of art. 10, § 7, and art. 11 are sufficiently interrelated in the sense that the increased funding allowed by the amendment to the Distribution Formula provides a means of

paying for the inflation increases. It is true that the proposed amendment of the Distribution Formula affects the other beneficiaries as well. Nonetheless, we would counsel not to file a lawsuit on this basis alone. The single-subject rule has been too variable in its application to justify the risk of a lawsuit of this magnitude.

D. Conclusion.

The proposed amendment of the Distribution Formula, if approved by the voters, cannot go into effect unless and until approved by Congress as well. A pre-election lawsuit cannot be filed on this basis, but a declaratory-judgment lawsuit can be filed to halt the implementation of the amendment, if passed at the election, until Congress authorizes it. We would advise against a pre-election challenge based on the single-subject rule as too risky.

Thank you for your attention to this matter.

Very truly yours,

CANTELME & BROWN, P.L.C.

By: David J. Cantelme

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